

TENNESSEE DEPARTMENT OF REVENUE
LETTER RULING #97-17

WARNING

Letter rulings are binding on the Department only with respect to the individual taxpayer being addressed in the ruling. This presentation of the ruling in a redacted form is informational only. Rulings are made in response to particular facts presented and are not intended necessarily as statements of Department policy.

SUBJECT

Whether, when performing a contract for a Tennessee municipality, [THE TAXPAYER] is subject to Tennessee sales and use tax when acting as a construction manager for the municipality and using the municipality's employees to install the materials purchased by the municipality.

SCOPE

This letter ruling is an interpretation and application of the tax law as it relates to a specific set of existing facts furnished to the Department by the taxpayer. The rulings herein are binding upon the Department, and are applicable only to the individual taxpayer being addressed.

This letter ruling may be revoked or modified by the Commissioner at any time. Such revocation or modification shall be effective retroactively unless the following conditions are met, in which case the revocation shall be prospective only:

- (A) The taxpayer must not have misstated or omitted material facts involved in the transaction;
- (B) Facts that develop later must not be materially different from the facts upon which the ruling was based;
- (C) The applicable law must not have been changed or amended;
- (D) The ruling must have been issued originally with respect to a prospective or proposed transaction; and
- (E) The taxpayer directly involved must have acted in good faith in relying upon the ruling and a retroactive revocation of the ruling must inure to his detriment.

FACTS

The Taxpayer, a well-established general contractor, has done business in Tennessee since [YEAR]. The corporation has performed numerous projects for Tennessee municipalities. Such projects include schools, jail facilities, and public works buildings. The Taxpayer states that, in most cases, it has acted as what it calls a “construction manager” in constructing these projects. The Taxpayer proposes to perform its municipality construction contracts as a construction manager for the municipality involved and to use only employees of the municipality to install materials and perform all work pursuant to completion of its contract with the municipality.

ISSUES

Will The Taxpayer be subject to Tennessee sales and use tax if it performs its municipality construction contracts acting as a construction manager and using only municipal employees?

RULINGS

Yes. However, under certain circumstances, The Taxpayer may not be liable for the tax. The factors that the Department of Revenue would consider in making this determination are set forth in the Analysis section of this Letter Ruling.

ANALYSIS

A Contractor Who Uses Tangible Personal Property In The Performance Of A Tennessee Municipal Contract Is Subject To Tennessee Sales And Use Taxes

T.C.A. § 67-6-329(a)(13) exempts all sales made to the State of Tennessee, or any county or municipality within the state, from Tennessee sales and use taxes. Therefore, a Tennessee municipality may purchase materials and supplies to be used in construction of a school, jail facility, municipal building or other municipal project without being subject to Tennessee sales or use tax on such items.

T.C.A. § 67-6-209(b) makes the following provisions concerning contractors who, in performance of their contracts, use tangible personal property not previously subjected to sales or use tax.

Where a contractor or subcontractor hereinafter defined as a dealer uses tangible personal property in the performance of the contract, or to fulfill contract or subcontract obligations, whether the title to such property be in the contractor, subcontractor, contractee, subcontractee, or any other person, or whether the title holder of such property would be subject to pay the sales or use tax, . . . except where the title holder is a church, private nonprofit college or university and the tangible personal property is for church, private nonprofit college or university construction, such contractor or subcontractor shall pay a tax at the rate prescribed by § 67-6-203 measured by the purchase price of such property, unless such

property has been previously subjected to a sales or use tax, and the tax due thereon has been paid. The exemption provided for herein for private nonprofit colleges or universities shall apply only to the state portion of the sales tax. The sales or use tax levied by this chapter shall not apply to carpet installed for a church when the church is exempt from sales or use taxes under § 67-6-322.

Under T.C.A. § 67-6-209(b), a contractor who uses tangible personal property in performance of a contract with a Tennessee municipality must pay Tennessee use tax on the materials and supplies so used even though they have been purchased tax free by the municipality. Under the facts presented, The Taxpayer can not avoid payment of the Tennessee use tax on materials and supplies used in performance of its contract with a Tennessee municipality even though city employees are used to perform all work pursuant to completion of the contract. This is true because the contractor is the one responsible for performing the contract and thus, is the one who uses, in performance of such contract, the materials and supplies purchased tax free by the municipality.

A Tennessee Municipality May Purchase Materials and Supplies And Use Them On Municipal Projects Without Paying Either Sales Or Use Tax

Since T.C.A. § 67-6-329(a)(13) exempts all sales made to any county or municipality within the State of Tennessee from Tennessee sales and use taxes, a Tennessee municipality can purchase materials and supplies, or other tangible personal property, and use its own employees to construct, install, or fabricate such property for a municipal project without being subject to Tennessee sales and use taxes.

In the event The Taxpayer does not contract with a municipality to perform or be responsible for any work involving the use of tangible personal property to fulfill contract obligations and all of The Taxpayer's officers, managers, supervisors and other employees who work on a municipal construction project became bona fide employees of the municipality and are used by the municipality to complete its construction project, no sales or use taxes would apply to the materials and supplies, or other tangible personal property used in connection with the municipal construction project.

The Taxpayer can not avoid the Tennessee sales and use tax by simply having the municipality pay its officers, managers, supervisors and other employees who work on the municipal project. The Taxpayer will be a contractor subject to Tennessee sales and use tax unless it does not contract with a municipality to perform or be responsible for any work involving the use of tangible personal property to fulfill contract obligations and all of its officers, managers, supervisors and other employees who work on the municipal project are bona fide employees of the municipality. In making a determination on issues of this nature, the Department of Revenue will consider whether the following facts are present and will also consider any additional facts that may be applicable to a taxpayer's particular situation.

1. The Taxpayer does not contract with the municipality to perform any work involving the use of tangible personal property to fulfill its contract obligations.
2. The Taxpayer does not provide the municipality a performance bond and does not otherwise express terms by which it becomes financially responsible for the quality or time of completion of the construction project.
3. The Taxpayer does not provide the equipment and tools used in the construction unless they are leased to the municipality under a written lease, the provisions of which are actually performed by both parties and which reflects at least the customary market lease rates for similar equipment and tools.
4. The Taxpayer does not control the details of the municipal construction project or otherwise function as a contractor for the project.
5. All persons who are, or who have been, officers, managers, supervisors or other employees of The Taxpayer and who work on the municipal project must be on the municipality's payroll, be paid by the municipality for the work they do on the project, and be controlled by the municipality.
6. The municipality involved must provide the same employee benefits, such as insurance coverage, retirement plans, vacation time, sick leave, holidays, etc., to all persons who are or have been officers, managers, supervisors or other employees of The Taxpayer but who are now on the payroll of the municipality and who work on the municipal project.

If The Taxpayer meets the criteria set forth above, T.C.A. § 67-6-209(b) will not be applicable and The Taxpayer will not be liable for use tax on tangible personal property purchased by a Tennessee municipality and used in a municipal construction project.

Arnold B. Clapp, Senior Tax Counsel

APPROVED: _____
Ruth E. Johnson, Commissioner

DATE: 6-2-97